S T A T E O F M I C H I G A N

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the Matter of the Application of **The Detroit Edison Company** for Authority to Implement a Power Supply Cost Recovery Plan in its Rate Schedules for 2011 Metered Jurisdictional Sales of Electricity.	))))))	Case No. U-16434

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on September 30, 2011.

Exceptions, if any, must be filed with the Michigan Public Service Commission, P.O. Box 30221, 6545 Mercantile Way, Lansing, Michigan 48909, and served on all other parties of record on or before October 17, 2011, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before October 31, 2011. **The Commission has selected this case for participation in its Paperless Electronic Filings Program. No paper documents will be required to be filed in this case.**

At the expiration of the period for filing exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

MICHIGAN ADMINISTRATIVE HEARING SYSTEM
For the Michigan Public Service Commission

Mark Eyster

Digitally signed by Mark Eyster
DN: cn=Mark Eyster, c=US, email=eysterm@michigan.gov
Date: 2011.09.30 12:36:51 -04'00'

Mark D. Eyster
Administrative Law Judge

September 30, 2011
Lansing, Michigan

S T A T E O F M I C H I G A N

MICHIGAN ADMINISTRATIVE HEARING SYSTEM

FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the Matter of the Application of	)	
The Detroit Edison Company for	)	Case No. U-16434
Authority to Implement a Power Supply	)	
Cost Recovery Plan in its Rate	)	
Schedules for 2011 Metered	)	
Jurisdictional Sales of Electricity.	)	

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

On September 30, 2010, The Detroit Edison Company (Edison, the Company, or DECO) filed this application requesting authority from the Michigan Public Service Commission (Commission) to implement a Power Supply Cost Recovery plan (Plan) in its rate schedules for 2011 metered jurisdictional sales of electricity.

On December 2, 2010, a pre-hearing conference was held before Administrative Law Judge, Mark D. Eyster. Counsel appeared on behalf of Edison, the Michigan Public Service Commission staff (Staff), the Michigan Community Action Agency Association (MCAAA), the Attorney General, the Michigan Environmental Council (MEC), and the Association of Businesses Advocating Tariff Equity (ABATE). At the pre-hearing conference, intervenor status was granted to ABATE, MCAAA, MEC, and the Attorney General. An evidentiary hearing was conducted on May 19, 2011. Briefs were filed on

June 10, 2011, and reply briefs were filed on June 28, 2011. The record in this matter consists of a transcript, 311 pages in length, and 43 exhibits.

FINDINGS OF FACT

Introduction

Edison presented the testimony of eight witnesses: Robert A. Gailliez, Supervisor – Reactor Engineering; Michael G. Hoffman, Supervisor, Business Development, Fuel Supply; Kenneth D. Johnston, Regulatory Consultant; Michael W. Shields, Manager – Wholesale Market Developments, Regulatory Affairs; Sherrie L. Siefman, Supervisor of Long Term Energy Forecasting; Angela P. Wojtowicz, Supervisor Midterm Optimization Group; James J. Musial, Manager of Federal Regulatory Affairs at DTE Energy Corporate Services, and; Wayne A. Colonnelo, Director of Nuclear Support.

Mr. Gailliez presented direct testimony to support Edison's five-year projection of nuclear fuel expense. He sponsored Exhibit A-1. Mr. Hoffman presented testimony to address fossil fuel expenses. He sponsored Exhibit A-2. Mr. Johnston presented direct testimony to provide the calculation of the monthly PSCR billing factors for 2011 and projected average annual PSCR billing factors for 2012 through 2015. He also presented rebuttal testimony related to Edison's Reduced Emissions Fuel (REF) expenses. He sponsored Exhibits A-3, A-4, and A-21 through A-23. Mr. Shields presented testimony addressing projected expenses related to services provided by ITC Transmission (ITC) and related to its participation with the Midwest Independent Transmission System Operator

(MISO). He sponsored Exhibits A-5 through A-7. Ms. Siefman presented testimony addressing Edison's sales and system output forecasts for 2010 through 2015. She sponsored Exhibits A-8 through A-12. Ms. Wojtowicz presented direct testimony regarding Edison's projected generation, emissions and associated emission allowance expenses, and purchase power expenses for 2011 through 2015. She presented rebuttal testimony to address the Attorney General's concerns regarding Edison's competitive solicitations for capacity. She sponsored Exhibits A-13 through A-20. Mr. Musial presented direct testimony about Federal Energy Regulatory Commission (FERC) matters that may affect Edison's cost of services. Mr. Colonnello presented rebuttal testimony in response to the MCAAA's testimony regarding spent nuclear fuel (SNF) and establishment of a SNF trust. By stipulation of the parties, Exhibit A-24 was admitted into evidence.

The Attorney General presented the testimony of Michael J. McGarry, President and CEO of Blue Ridge Consulting Services, Inc. Mr. McGarry's testimony addressed Edison's projected use of activated carbon to reduce mercury emissions and concerns regarding Edison's compliance with its code of conduct. Mr. McGarry sponsored Exhibits AG-1 through AG-3.

MCAAA presented the testimony of two witnesses: Ronald C. Callen, a consultant and technical advisor, and William A. Peloquin, a Certified Public Accountant. Mr. Callen presented testimony related to the federal government's failure to meet its obligations for SNF disposal and his recommendation that the Commission require Edison to deposit SNF Standard Contract fees into an

MPSC regulated trust. Mr. Callen sponsored Exhibits MCAAA-1 through MCAAA-10. Mr. Peloquin presented testimony to address ring-fencing, Edison's REF proposal, NO_x allowance expenses, and a proposed Spent Nuclear Fuel Trust Fund. He sponsored Exhibits MCAAA-11 and MCAAA-12. In addition, pursuant to a stipulation of the parties, Exhibit MCAAA-13 through MCAAA-15 were admitted into evidence; MCAAA-14 for the limited purpose of "background information only". 2 Tr 308.

PSCR Billing Factors

Edison has calculated a 2011 levelized monthly PSCR billing factor of negative 2.98 mills/kWh. 2 Tr 58. Exh A-3. The calculations are based on the change in the average unit cost of power supply from the base of 31.26 mills/kWh. 2 Tr 58. The 2011 Plan includes an estimated under-recovery of $36.349 million from the 2010 PSCR period. 2 Tr 68.

Fermi-2 Nuclear Fuel Expense

There are three components of nuclear fuel expense: front end costs, in-core interest expense, and regulatory costs. 2 Tr 26. Front end costs include the costs of the uranium ore, its conversion to uranium hexafluoride, enrichment services, and fabrication of fuel bundles. 2 Tr 22-27. These costs are amortized to PSCR expense over the life of the fuel. 2 Tr 27. Edison does not incur in-core interest expenses. 2 Tr 27.

Edison currently incurs $1/MWh of net electrical generation sold in regulatory costs. "Edison considers the $1.00/net MWh sold to be compensation to the [Department of Energy (DOE)] for executing its responsibilities and obligations in accordance with the standard contract for disposal of SNF and Title 10, Part 961 Appendix G." 2 Tr 27. As stated by Edison, at 2 Tr 28:

> Under the contract and law, the primary responsibility of the DOE is to accept title to the SNF and provide for its transportation from Fermi 2 to the disposal site. In this regard, the DOE is responsible for providing the shipping cask and its handling procedures, any special tools or equipment necessary to handle the cask, and routine cask maintenance.
>
> The DOE is not responsible for the preparation and packaging of the SNF, or for the loading of the shipping cask. Additionally, the DOE is not responsible for any incidental maintenance, protection, or preservation of the cask while it is in the possession and control of Detroit Edison. The fees paid by Detroit Edison to the DOE are deposited into the Nuclear Waste Fund, as required by Public Law 97-425, and the fee may be adjusted from time to time in accordance with the law to ensure full cost recovery by the DOE.

Exhibit A-1 provides the following projected nuclear fuel expense:

Years 2011–2015
($000)

Year	GWHr	Fuel Amort	In-core Interest	Regulatory Cost	Nuclear Fuel Exp	$/MWHr	Cents/ MBTU
2011	9,579	48,031	0	8,842	56,873	5.94	57.7
2012	8,913	47,387	0	8,226	55,613	6.24	62.2
2013	8,931	48,907	0	8,243	57,150	6.40	64.3
2014	9,732	56,335	0	8,983	65,318	6.71	67.5
2015	8,927	53,667	0	8,239	61,906	6.94	69.7

For a number of reasons, Edison's witness, Mr. Gailliez considers these expenses reasonable and prudent. See 2 Tr 31.

The MCAAA's witness, Ronald C. Callen, provided testimony expressing his opinion on three related areas: a history of the federal government's response to the issue of SNF disposal, a "demonstration that [Edison's] actions . . . have been insufficient and inadequate, and therefore unreasonable and imprudent, in responding to the federal government's failure to meet its obligations", and his recommendation that Edison "place quarterly payments of SNF Standard Contract fees collected from ratepayers into an external interest bearing, MPSC-regulated trust." 2 Tr 259-60.

In 1982 Congress passed the Nuclear Waste Policy Act. As stated by Mr. Callen, at 2 Tr 266-67:

> The Act recognized that the proper storage and disposal of nuclear waste was a national responsibility. The Act also established an essential statutory bargain that would provide for the generators of nuclear energy to pay the cost for a storage or disposal program in exchange for the federal government's commencing the disposal of nuclear waste by a date certain, January 31, 1998 . . . . Congress vested the DOE with the responsibility of developing the nuclear waste facilities.
>
> * * *
>
> In 1983, DOE promulgated a single version of a Standard Contract outlining DOE's duties to accept nuclear waste by January 31, 1998, in exchange for the fee payments under the NWPA. All nuclear utilities, including DECO, were required to enter into the Standard Contract . . . . Upon establishing the Standard Contracts, the fee collections commenced in 1983.

After outlining the federal government's failure to take possession of SNF by January 31, 1998, Mr. Callen states, at 2 Tr 271-72:

> During the period 2000-2008, progress was made with respect to the SNF program. The DOE Secretary selected the Yucca Mountain site for characterization in 2002, a decision quickly adopted by President George Bush. The Congress in 2002 undertook action to approve the site for a license application . . . . In 2008, the DOE filed an extensive license application, which was accepted for filing by the Nuclear Regulatory Commission (NRC) and which became the subject of NRC proceedings in NRC Docket No. 63-001-16 HLW.
>
> . . . In 2009, the new administration commenced actions to dismantle the Yucca Mountain Program. By early 2010, the administration had proposed to discontinue appropriations for the program and filed a Motion to Stay the NRC proceedings on the

> License Application and filed a Motion to Withdraw the NRC License Application . . . .
>
> In its FY 2011 budget proposal, the Federal Administration released its decision that "the Administration has determined that developing a repository at Yucca Mountain is not a workable option and the nation needs a better solution **. . .** based on sound science. …" Together with funding changes that coalesce with its decision, the Yucca development program has been zeroed out. Accordingly, the Administration, also in the budget proposal, stated its intent to discontinue its [license application] to the NRC. . . .

Mr. Callen concludes with his opinion that the "present situation suggests that the federal government will never dispose SNF." 2 Tr 275.

Edison's witness, Mr. Colonnello, disagrees and states, at 2 Tr 193-94, that:

> The [DOE] has continued to acknowledge its obligation to accept spent nuclear fuel from Detroit Edison and other nuclear utilities.
>
> . . . While Yucca Mountain development has been suspended under the Obama administration, the President has also recently recommitted to nuclear power as a clean energy source. Furthermore, DOE Secretary Chu has on multiple occasions committed to meet the federal government's SNF obligations. SNF Storage is a national issue which the federal government has a statutory and contractual obligation to resolve and it is not unreasonable to expect that the federal government will eventually do so.
>
> Further, development of a repository is necessary not only for disposal of commercial spent nuclear fuel . . . but it is also important to our national security for the disposal of spent fuel generated from federal facilities and high level radioactive waste resulting from this nation's defense activities. Even putting aside the interest of commercial operators, the Federal government definitely has a significant incentive to ultimately dispose of its own Spent Nuclear Fuel and high-level radioactive waste.

At 2 Tr 280, MCAAA's Mr. Callen, expresses his opinion that Edison's response to the federal governments actions "appears to have been somewhat limited and inadequate." Mr. Callen adds, at 2 Tr 280-82, that:

> While I recognize that DECo filed a damage case in the U. S. Court of Claims, DECo has not provided . . . any evidence as to the status or progress of that case. Also, while DECo may also be participating in joint Court review of DOE's decision to continue to collect the fees at the present level, DECo has not revealed any further action it has undertaken to address the federal Administration's decision in 2010 to suddenly cease the program, to cut all appropriations, and to seek to withdraw the License Application for the Yucca Mountain repository. . . . DECO has not undertaken any . . . action to escrow the fees presently being paid, to seek restitution of past fees paid, or otherwise to enjoin or challenge the recent actions by the federal government.
>
> DECO has also not revealed or indicated that they have undertaken any adequate analysis of the obligations that may arise to DECO and possibly ratepayers as a result of the federal failures. At the very least, DECo's testimony in this case should have discussed and analyzed these issues. Instead, DECo has ignored the issue.
>
> * * *
>
> It is my conclusion that DECO has not demonstrated sufficient actions it has taken, or is actively considering, to fully protect itself from the federal government's default. The Commission should therefore determine that DECO has not been reasonable and prudent in the administration and enforcement of its Standard Contract with DOE. The Commission should therefore adopt certain remedies relative to the monies that DECO seeks in rates for the SNF fee payments.

Mr. Callen recommends the the SNF fees "be placed in an external MPSC regulated trust." 2 Tr 284. At 2 Tr 284-86, Mr. Callen continues:

> This trust . . . would receive the funds collected in rates equivalent to the present 1 [mill/MWh] fee which DECO pays to the federal government . . . . These escrowed funds would provide financial resources for a replacement disposal initiative if needed in the future, and would protect ratepayer interests in these funds.
>
> * * *
>
> A less desirable variant of this option is for . . . a partial escrow of the funds to a trust, subject to DECo providing a plan or report concerning its enforcement actions taken or planned. The Commission could later adjust the escrow amounts depending upon the adequacy of DECo's efforts.

In rebuttal, Edison's witness, Mr. Colonnello, opined that Edison has "been effective in managing nuclear fuel expenses." 2 Tr 186. He established that "Edison's nuclear fuel expenses have consistently been within the first and second quartile in the nuclear industry for similarly situated plants" and that "[t]hese fuel expenses include fees paid to the DOE." 2 Tr 186. Mr. Colonnello added his opinion that "[s]ince it became apparent that the DOE would not begin accepting SNF in the contractually mandated timeframe, Detroit Edison has taken a conservative and graduated approach to manage on-site spent fuel storage." 2 Tr 186. He continues at 2 Tr 187-190, by stating:

> [MCAAA] unreasonably proposes that SNF costs be treated differently than other costs incurred to preserve the continued economic operation of the Fermi 2 plant.
>
> * * *
>
> [Edison] has taken actions to protect its rights under the Standard Contract . . . and to protect itself and customers regarding DOE's partial breach of its Standard Contract. The Company's evaluation and consideration of various long-term options for SNF storage – which evaluation began in 1994 – demonstrates that it has been reasonable and prudent with respect to actions and associated costs for storing SNF. Moreover, Detroit Edison's actions have been and continue to be thoroughly consistent with the actions of other nuclear utilities.
>
> Along with other nuclear utilities, Detroit Edison is also engaged in initiatives through Nuclear Energy Institute (NEI). In addition, the Company has worked over the past several years to solicit grass roots support and congressional support for the various legislative efforts in the U.S. Congress to advance the acceptance of spent nuclear fuel at an interim storage facility.
>
> The NEI and 16 of its member companies, including Detroit Edison, filed a Joint Petition for Review in the U.S. Court of Appeals for the District of Columbia Circuit against the U.S. Department of Energy on March 8, 2011 seeking recalculation of the fee that consumers of electricity produced at nuclear energy facilities pay for the federal government's nuclear fuel management activities. This Petition was filed in parallel with a similar petition filed by the National Association of Regulatory Utility Commissioners.

Detroit Edison has actively prosecuted its case for breach of contract damages in the Court of Federal Claims and has been a member of a 21 utility litigation group dedicated to resolving the industry's claims.

The Company also evaluated various storage options (e.g., wet storage expansion, independent spent fuel storage installation (dry fuel storage)), for expanding the capacity for storing SNF onsite and compared the total life-cycle cost of various storage options. The Company's spent fuel storage strategy was to exhaust the reasonable wet storage capacity before building the Independent Spent Fuel Storage Installation facility. Phase 1 of the spent fuel pool expansion project was completed in 2001. Phase 2 of the spent fuel pool expansion activities was completed in 2007. The phased-approach for wet storage expansion provides balance between establishing timely storage capacity and preserving capital expenditures. This approach is consistent with industry experience and has minimized the costs of storing SNF onsite.

* * *

Edison's actions in pursuit of an SNF storage solution have been ongoing for almost two decades. The Company was one of 33 utilities that participated in the initial development of the Mescalaro Private Storage Project in April 1994. This alternative private SNF storage initiative was ultimately unsuccessful. In September 1995, Detroit Edison, PSE&G and GPU filed a lawsuit in the U.S. Court of Appeals for the District of Columbia Circuit against the DOE, arguing that the department had an unconditional legal responsibility to begin taking utility spent fuel by the 1998 contract acceptance date. Accompanying it was a motion asking the court to consolidate the case with several other lawsuits filed by 10 other utilities and 36 states and public utility commissions regarding the 1998 date. Then, in January 1997, the Company along with 35 nuclear utilities filed a suit in the U.S. Court of Appeals for the District of Columbia Circuit to attempt to compel the federal government to meet its legal obligation to begin accepting SNF. In August 2002, the Company filed suit against the DOE in the U.S. Court of Federal Claims regarding damages for a continuing, partial breach of contract associated with DOE's failure to begin acceptance of spent nuclear fuel on January 31, 1998.

At 2 Tr 192-93, Mr. Colonnello provides his opinion that:

Regardless of whether a separate trust fund is created, continued Fermi 2 generation . . . will still require submittal of the fee . . . to avert breach of [the Standard Contract] and potentially placing the Fermi 2 license in jeopardy. If Detroit Edison breached

> the contract, then it would also likely put current and future lawsuits against the DOE for damages in jeopardy.
>
> * * *
>
> Paying the DOE and escrowing an additional amount would also be unreasonable because [the] cost increase would not be in Edison's, or its customers', best interests. Furthermore, in light of Detroit Edison's prudent response to this national issue, it would be unreasonable and unjust for the Commission to deny Detroit Edison recovery of this additional cost in customer rates.

<u>Fossil Fuel Expense</u>

Exhibit A-2 is Edison's five year forecast of fuel expenses. The exhibit provides separate information for coal, No. 2 oil, No. 6 oil, natural gas, and coke oven gas (COG).

At 2 Tr 36-38, Edison's witness, Mr. Hoffman, described the method used to develop the fuel expense forecast, as follows:

> The 7 months actual, 5 months forecast (7&5 Outlook) for 2010 is the basis for the 2011-2015 forecast. The 7&5 Outlook uses actual August 1, 2010 inventory quantities and costs, and forecasts the remaining five months of 2010. The forecasted December 31, 2010 inventory quantities and costs are inputs to the 2011-2015 forecast.
>
> The forecasted delivered coal costs for the last five months in 2010 and for 2011-2015 were determined using existing contract coal prices and transportation rates, forecasted spot market coal prices, and forecasted transportation rates. The forecasted spot market coal prices for 2011-2013 were based upon market information obtained from an over-the-counter (OTC) coal broker. For 2014 and 2015, spot market coal prices were estimated to remain constant with 2013 prices. The forecasted transportation rates were calculated by applying forecasted rail cost adjustment factors (RCAF) obtained from Global Insights to existing and forecasted transportation rates.
>
> The forecasted delivered No. 2 and No. 6 oil and natural gas costs were determined by using the New York Mercantile Exchange (NYMEX) futures prices adjusted for basis and local distribution company (LDC) charges.

> The composite monthly delivered coal cost for each plant was calculated by using Fuel Supply's Fuel Price Estimating (FPE) spreadsheet for the balance of 2010 and 2011-2015. The FPE applies existing and forecasted coal prices and transportation rates to the monthly delivery requirements for each plant. The coal delivery requirements are determined by subtracting actual coal pile inventory levels from the coal pile inventory level targets and adding the coal consumption requirements . . . . Delivery requirements for oil and gas are determined in a similar manner.
>
> The average annual unit cost of coal delivered to each Detroit Edison generation plant that burns coal was calculated in each year's FPE. The FPE output and delivered oil and gas delivery requirements and costs are used as inputs to the Forecasting Information and Budgeting System (FIBS) spreadsheet. Fossil fuel expense was calculated in FIBS by multiplying the average cost of inventory by fuel consumed.

Edison plans to meet its coal requirements with a combination of "long-term and spot market purchases." 2 Tr 38. A summary of the long-term contracts is provided at 2 Tr 39. No. 2 oil is expected to be provided pursuant to contracts based on spot index price and are no more than two years in duration. 2 Tr 39. No. 6 is expected to be supplied under spot market agreements of no more than one year in duration. 2 Tr 39. Edison's natural gas will be supplied "through a combination of . . . local distribution companies . . . , spot market purchases and one long term . . . supply agreement based on a spot index price." 2 Tr 39-40. Edison purchases COG from EES Coke Battery, LLC under an agreement that began in June, 2009. 2 Tr 40.

"A significant increase in forecast coal expense in 2011 is due to the replacement of [a 13-year] rail transportation agreement that expire[d] on December 31, 2010, with a new rail transportation agreement [that began] January 1, 2011." 2 Tr 41. Mr. Hoffman indicates that the "only other known factor that could affect fuel cost is the Reduced Emission Fuel Project . . . at

Edison's Belle River and St. Clair Power Plants." 2 Tr 44. As explained in more detail, below, the Reduced Emission Fuel Project is a process that applies chemical additives to coal to produce "Reduced Emission Fuel" (REF). 2 Tr 44. "The [REF] is expected to reduce SO_2, mercury (Hg) and NO_X emissions and therefore the related emission allowance expense . . . . The additive [and] coal that it is . . . applied to will be purchased by Edison from affiliated companies". 2 Tr 44-45. The PSCR cost of the chemical additives applied to the coal (adder) will be the lower of the PSCR benefit of reduced SO_2 and mercury emissions associated with the consumption of the REF or the revenue requirement associated with the REF Project production facility. 2 Tr 45. "The level of SO_2 emissions reductions . . . result in [adder costs] of $53,528, $20,125, $13,643, $9,160 and $25,737 respectively, in the forecast years 2011 – 2015. In addition, the 2015 [adder] cost includes $9.9 million associated with avoided mercury emissions expense. The forecast [adder] costs appear on line 5 of Exhibit A-2." 2 Tr 46.

For a variety of reasons, found at Tr 2, p 46-48, Mr. Hoffman believes "Edison's present fuel supply policy, objectives, and strategies . . . are reasonable and prudent." Tr 2, p 48.

<u>NO_X</u>

Edison projects average NO_X Ozone Season Emission Allowance costs of $24.29 for 2011, $4.92 for 2012, $5.61 for 2013, $5.27 for 2014, and $5.98 for 2015. Exh A-17. Of the total seasonal allowances projected for use in 2011, 500 were purchased prior to the year at an expense of $367,500 or $735 per allowance. Exh A-17. 2 Tr 302. For 2011, Edison projects a need to purchase an additional 3548 seasonal allowances at a cost of $80,444 or $22.67 per allowance. Exh A-17, 2 Tr 302.

Edison projects average NO_X Ozone Annual Emission Allowance costs of $127.66 for 2011, $11.78 for 2012, $7.54 for 2013, $5.50 for 2014, and $7.38 for 2015. Exh A-18. Of the annual allowances projected for use in 2011, 1250 were purchased prior to the year at an expense of $3,278,750 or $2,623 per allowance. Exh A-18. 2 Tr 302. For 2011, Edison projects a need to purchase an additional 8662 annual allowances at a cost of $2,118,895 or $245 per allowance. Exh A-18. 2 Tr 302. An additional 32,292 allowances are allocated from the EPA. Exh A-18.

Because of the projected availability of lower priced allowances in 2011, MCAAA's witness, Mr. Peloquin, recommends a reduction of Plan expenses in the amount of $3,319,170. 2 Tr 304. This figure represents the difference between the cost of allowances purchased before 2011 and the projected cost for the same allowances, if purchased in 2011. 2 Tr 303.

In response to Mr. Peloquin, Edison's witness, Ms. Wojtowicz testified, at 2 Tr 216-17, that:

> The Company purchased NO_x seasonal and NO_x annual emission allowances for 2011 in the year 2008 in accordance with its pre-purchase strategy set forth in the Company's 2008 PSCR Plan Case No. U-15417. Under the pre-purchase strategy, the Company purchased a portion of it[s] projected emission allowance requirements to allow adequate lead time to adjust the control technology construction schedule in the event of significant changes in the availability and/or the market prices of emission allowances. As described in its 2008 PSCR Plan, the Company purchased a

> portion of its 2011 NO_x seasonal and NO_x annual emission allowances in 2008 at then-current market prices for 2011.
>
> * * *
>
> In July 2008, the D.C. Circuit Court vacated the Clean Air Interstate Rule (CAIR), ... NOx emission allowance prices dropped significantly after CAIR was vacated. In late 2008, the U.S. economy went into a deep recession, which resulted in decreased electricity demand. Because of this decrease in demand, the U.S. generating plants operated less and emitted less NOx. The excess supply of NOx emission allowances caused the decrease in price. These recent events that caused NOx emission allowance prices to decrease were unpredictable and validate the Company's "dollar cost averaging" approach to emission allowance acquisition. NOx emission allowance prices have been very volatile since 2008 with annual NOx emission allowances ranging from as high as about $5600 all the way down to the current low of about $250. In that same period, seasonal NOx allowances have been as high as about $1400 and as low as about $25.

There being no evidence to the contrary, Mr. Wojtowicz's testimony is accepted as fact.

<u>Reduced Emissions Fuel Project</u>

In this filing, Edison is proposing a Reduced Emissions Fuel Project (Project) for its Belle River Power Plant (BRPP) and its St. Clair Power Plant (SCPP). Edison began the Project in January, 2011. 2 Tr 200. Under the Project, Edison will sell, at book costs, a portion of its coal inventory to the Belle River Fuels Company (BRFC) and the St. Clair Fuels Company (SCFC) (collectively, the Fuels Companies). 2 Tr 62. DTE Energy Services (DTEES) is the "parent company of the Fuels Companies" and holds "a license to use [a] unique and proprietary chemical additive technology" to treat coal "at DTE Energy sites". The Fuels Companies will "apply chemical additives to the coal". 2 Tr 158. "The additive itself, as well as the western coal that it is to be applied to, will be purchased by Edison from [the] affiliated . . . Fuels Companies". 2 Tr 45. Use of REF reduces SO_2 emissions. 2 Tr 158. Edison, also, expects the REF to reduce NO_X emission allowance expenses. 2 Tr 64. However, because of the "variability of NO_X emissions, this cost reduction cannot be precisely estimated". 2 Tr 64. Any such NO_X emission reduction "benefits will flow directly to the PSCR customer". 2 Tr 46. More importantly, as explained below, the primary purpose for the project is to lower the cost of mercury emission reductions mandated to begin in 2015.

Edison's witness, Mr. Johnston, testified that there are a number of reasons that Edison entered into the arrangements with the Fuel Companies. He states that the arrangements offered Edison "a risk free option" to address the mercury emission reduction requirements contained in Michigan Rule 1503. According to Mr. Johnston, "Edison reasonably determined that the tax risks and commitment to a technology that was unproven at its generating facilities were not appropriate for a regulated utility." 2 Tr 204. He adds, at 2 Tr 205-06, that:

> [DTEES] . . . has experience designing, constructing, and operating the production equipment and was willing to take on the associated risk. At the time the REF facilities were constructed at the Belle River and St. Clair Power Plants, the existing legislation required the facilities to achieve commercial operation by January 1, 2010 and Detroit Edison had only a limited time to pursue alternative processes or suppliers. Further, Detroit Edison was not aware of any other supplier that was willing to make this type of investment at the time the REF project needed to move forward given the existing legislation.
>
> In addition, at the time that Detroit Edison entered into discussions with DTEES for the provision of REF for Belle River Power Plant, DTEES was one of only three known licensees for the provision of the proprietary technology and DTEES held a license to use the unique and proprietary chemical additive technology at Detroit Edison sites. DTEES had been evaluating Hg technologies

> for more than two years and through August 2009 made a significant investment in the evaluation and testing of multiple technologies.
>
> * * *
>
> It made sense [for Edison to move forward with the Project with DTEES because] DTEES had already reached a similar agreement with the Michigan Public Power Agency (MPPA), a partial owner of the Belle River Power Plant. In addition, the DTEES proposal provided the following:
>
> (a) Reduction in Detroit Edison's working capital expense by not carrying coal inventory;
>
> (b) Reduction in NO_X emission allowance expense; and
>
> (c) PSCR customers will never pay more than their environmental benefits.

Starting in 2015, Edison plans to use both Standard Powdered Activated Carbon (PAC) and Brominated Activated Carbon (BrPAC) sorbents to reduce mercury emissions. 2 Tr 158. Edison believes that both PAC and BrPAC should be considered a PSCR disposal cost under MCL 460.6j(1)(a), similar to the Commission's treatment of urea costs. 2 Tr 198. Edison projects PAC to be substantially less expensive than BrPAC. 2 Tr 158. The REF enables Edison to substitute PAC for BrPAC, thus reducing mercury sorbent expenses. 2 Tr 158. With use of REF, Edison projects a reduction of mercury sorbent expense for 2015. 2 Tr 158. Exhibit A-20. Pursuant to MCL 460.6j(7), Edison "is seeking the Commission's concurrence that it is likely to permit the Company to recover the mercury emission-related expense for 2015." Application, p 4.

The Fuels Companies have already constructed REF facilities on the Belle River Power Plant and St. Clair Power Plant sites and "integrated" them into Edison's coal delivery process. 2 Tr 63. Edison will provide "coal handling and consulting and other services" to the Fuels Companies at "Edison's cost". 2 Tr 63. After processing, the Fuels Companies will provide REF to Edison on a "'just in time' delivery basis". 2 Tr 63. Under the project, Edison will have no "capital assets and O&M expenses for purposes of setting rates." 2 Tr 209. However, such costs "could in fact be recovered through charges of SCFC."[1] 2 Tr 209. "All costs incurred in processing the coal through the REF facility owned by the SCFC occur before the REF is delivered to Detroit Edison". 2 Tr 209. Reduced Emission Fuel will be sold to SCFC "at the original fully allocated cost at which [Edison] sold the coal to SCFC plus an REF adder." 2 Tr 202.

> The REF adder will consist of several components: (1) an adjustment amount related to fly ash disposal costs designed to keep Detroit Edison whole for any incremental fly ash disposal costs (beginning in January 2011), (2) an adjustment amount related to fly ash revenue (beginning in January 2015), (3) an adjustment amount based upon and no greater than Detroit Edison's reduction in actual SO_2 emission allowance expense (beginning in January 2011), and (4) an adjustment amount based upon Detroit Edison's reduction in actual mercury emission expense and capped at SCFC's revenue requirement (beginning in January 2015). 2 Tr 202.
>
> Since the fuel expense at the Belle River Power Plant is used in determining the following year's purchase power prices for the P.A.2. contracts, the increase in fuel expense due to the use of Reduced Emissions Fuel will result in a higher purchase power price. The REF price will be adjusted to ensure that this increased expense does not result in increased PSCR expense, all else being equal. 2 Tr 159.

Edison is proposing that, beginning in January, 2011, the adder component for reduced SO_2 emission allowance expense be recovered through the PSCR, as a fuel cost. 2 Tr 202. Edison proposes that, beginning in January, 2015, the adder component for reductions in mercury emission expense be

[1] Much of Edison's testimony specifically addressed the operations of and arrangements with SCFC. It is unclear whether the same descriptions apply to BRFC.

recovered through the PSCR, as a fuel cost, provided the Commission finds that both PAC and BrPAC are recoverable PSCR fuel disposal costs. 2 Tr 202. Under this arrangement, the price that SCFC is selling the adder to SCPP is the lower of SCPP's environmental benefit or SCFC's fully allocated cost. 2 Tr 203. Therefore, Edison's REF expense "will never exceed the financial benefits of reduced SO_2 and mercury emissions". 2 Tr 158. "To the extent . . . the REF . . . provides one of [Edison's] affiliates the potential to recover its revenue requirement for the REF facilities it has constructed, the basis for calculating the return on their 'rate base' is . . . Edison's currently authorized overall ROR of 7.02%". 2 Tr 206.

It appears unclear what Edison projects the adder costs to equal. At 2 Tr 46, Mr. Hoffman states that:

> The level of SO_2 emissions reductions . . . result in a [REF adder] cost of $53,528[2], $20,125, $13,643, $9,160 and $25,737 respectively, in the forecast years 2011 – 2015. In addition, the 2015 [REF adder] cost includes $9.9 million associated with avoided mercury emissions expense. The forecast . . . costs appear on line 5 of Exhibit A-2.

However, in exhibit A-21, line 7, Edison projects SO_2 emission allowance cost reductions of $12,348, $5,600, $3,801, $2,424, $2,534 for the years 2011-2015, respectively, and, on line 8, Edison projects a mercury sorbent cost reduction of $5,427,365 for 2015.

In January, 2011, the burning of reduced emission fuel at SCPP produced no measurable reduction in SO_2 emissions. 2 Tr 200. In February, 2011, the

[2] At 2 Tr 158, Edison's witness, Ms. Wojtowicz, provides a slightly different 2011 estimate when she states, "[t]he SO_2 emissions are projected to be 3509 tons less in 2011 from the use of REF with an associated reduction in SO_2 allowance expense of $52,528 as shown on Exhibit A-19."

REF, at SCPP, reduced SO_2 emission allowance expense by $1,035. 2 Tr 200. During these months the cost, to Edison, of the REF was equal to the SO_2 emission allowance expense savings. 2 Tr 200. Because of the increased costs of disposing of additional fly ash created by the REF, SCFC was required to pay $2,359. 2 Tr 200.

Edison "continues to evaluate REF as an alternative to . . . obtaining SO_2 and NO_X emission allowances and [as a means to] minimize the costs associated with reducing mercury . . . emissions at its Belle River and St. Clair Power Plants." 2 Tr 61. The REF "is in the early testing phases and the optimal proportion of chemical additives to fuel burned has not yet been determined." Exh AG-1.

MCAAA's Mr. Peloquin testified in opposition to the REF Project. He states that, "in [his] opinion", it "is not a category of expense to be included in a PSCR Plan." 2 Tr 300. Mr. Peloquin views the proposal as a means to "generate excess SO_2 allowances for sales" at a time when "Edison does not need to <u>purchase</u> SO_2 allowances for the consumption of coal." 2 Tr 300. At 2 Tr 300, Mr. Peloquin states his belief that the "REF proposal would set a number of poor ratemaking precedents" and adds:

> The REF proposal would endorse Edison's sale of utility coal to affiliates at Edison's book cost. The Commission historically has required the sale of utility property to be at the higher of the utility's cost or market prices. . . . Another troubling precedent is Edison's purchase of [REF] from its subsidiaries at a price greater than their out-of-pocket cost. Note that the cap on price of the REF project is the affiliates' "revenue requirements associated with the REF." . . . Thus, the Fuel[s] Companies will be selling refined coal to Detroit Edison at a profit. Also, DTE Energy Services is going to make a return (income) on its "coal refinement technology.". . . Edison's

> REF proposal would set a precedent of this Commission's approval of a utility purchasing a product from an affiliate at cost plus a profit.

The Attorney General’s witness, Mr. McGarry, also opposes the Project. In his opinion, Edison’s REF costs “are neither booked costs of fuel burned nor booked costs of purchased and net interchanged power transactions that can be recovered as PSCR expenses.” 2 Tr 225. Mr. McGarry believes “it would be premature for the Commission to pre-approve expenses that will not be incurred in the 2011 PSCR plan period” and that Edison should demonstrate that the Project complies with the Code of Conduct. 2 Tr 225.

In response, Edison’s witness, Mr. Johnson testified that the “single largest benefit for Detroit Edison from implementing this project is the ability to reduce mercury reduction compliance costs beginning in 2015, the first compliance year for Michigan Rule 1503.” 2 Tr 211. He acknowledges that “Section III.C of the Code of Conduct . . . provides for sales to affiliates at the higher of fully allocated cost or market price” and that the coal sold to SCFC is being sold below market price. 2 Tr 201. He adds, “SCFC will simply use the coal to produce REF and sell the REF back to . . . Edison for consumption at the SCPP”. 2 Tr 201. “[A]ny adjustments to the sale price will only serve to increase the resale price to . . . Edison.” 2 Tr 201. Mr. Johnson argues that “[b]ased upon the fact that the asymmetrical pricing provision of the Code of Conduct is intended to prevent . . . Edison from subsidizing its unregulated affiliates, it is clear that this transaction is consistent with that intent and effectuates the proper outcome.” 2 Tr 201.

ITC and MISO Expenses

At 2 Tr 81-114, Edison's witness, Mr. Shields testifies about "Edison's projected expenses associated with being a network transmission customer of ITC Transmission and with being a Market Participant of the Midwest Independent Transmission System Operator". Mr. Shields testimony addressed projected expenses for 2011 through 2015 and was divided onto two sections; Base Transmission charges and charges related to participation in the MISO Energy and Ancillary Services Markets. 2 Tr 81. Mr. Shields projects 2011 total Base Transmission costs of approximately $264.8 million. 2 Tr 92. He estimates 2011 MISO Energy and ASM Markets costs of approximately $7.4 million. 2 Tr 111. Mr. Shields adds, at 2 Tr 114, that:

> [These expenses] are necessary and integral to Detroit Edison being able to provide retail electric service to its full service customers. The rates upon which the expenses are determined are subject to approval by FERC and comply with FERC's vision for the operation and expansion of the interconnected electric transmission grid.

Mr. Shields' testimony stands uncontested, appears reasonable, and is accepted.

Sales and Output Forecasts: 2010-2015

At 2 Tr 120-135, Edison's witness, Ms. Siefman provided testimony to address Edison's electric sales and system output forecasts for 2010 through 2015. Ms. Siefman forecasts electric sales to decrease from temperature normalized sales of 48,280 GWh in 2009 to 46,874 GWh in 2015. 2 Tr 122. For the 2009 to 2012 period, she projects an average annual decrease in Residential Class sales of 2.3%; in Commercial Class sales of 1.1%, and; in Other Class sales of 16.4%. 2 Tr 122-23. For the same period, average annual Industrial Class sales are expected to increase by 5.7%. 2 Tr 123. Weather sensitive sales projections were made using average 1971 through 2000 mean daily temperatures at Detroit Metropolitan Airport. 2 Tr 134.

Ms. Siefman explains development of her forecast, by stating, at 2 Tr 123-24:

> For most sectors of the forecast, electric sales levels are related to the various economic, technological, regulatory, and demographic factors that have affected them in the past. The procedure begins with the assembly of historical data relating to the various sectors of the forecast. These data are examined and the factors that are statistically significant in explaining electric sales are identified using regression techniques. The forecast is developed employing the appropriate regression equations.
>
> Economic driving variables (explanatory factors), such as car and truck production, steel production, employment, and others, are entered into the regression equations to calculate projected future electric sales levels.
>
> The forecast is developed separately for each of four main categories: manufacturing, non-manufacturing, Residential Class, and Other Class. Sales in the manufacturing sector are forecast by developing subcategory equations for the automotive industry, the steel industry, chemicals, petroleum, metal fabrication, manufacturing equipment, rubber and plastics, non-metal processing, mining and other manufacturing. Modifications are made, as required, for displacement by customer self-generation in the manufacturing sectors. The non-manufacturing category is forecast using regression equations for nine subcategories. The subcategories are then disaggregated into markets. The non-manufacturing sales for each market are divided into Primary Class and Commercial Class components.
>
> In the Residential Class, an end-use approach is employed in which 38 different appliances or appliance groups are defined. The individual appliance forecasts that result are then aggregated to constitute the total Residential Class sales forecast. The Other Class is forecast by separating the class into wholesale-for-resale,

> municipal water pumping, and street lighting. System output is forecast as the sum of the electric sales values and the projected losses.

Ms. Siefman's testimony stands uncontested, appears reasonable, and is accepted.

Federal Energy Regulatory Commission (FERC) Issues

Edison presented the testimony of Mr. James J. Musial, at 2 Tr 164-181. He provided an "overview" of certain matters being addressed by FERC that may effect Edison's PSCR charges and Edison's activities related to those matters. Specifically, Mr. Musial addressed: the "Midwest ISO's proposal to establish a new MVP transmission planning and cost allocation category"; the "Midwest ISO's review of qualifying criteria associated with transmission projects that provide economic value (RECB III Phase 3)"; the "Midwest ISO's stakeholder process addressing generation resource adequacy requirements", and; "MISO's Transmission Expansion Plan (MTEP 10)". 2 Tr 164. No party contested any of Mr. Musial's testimony and it is accepted as fact.

Generation, Emissions, and Purchase Power Requirements: 2011 through 2015.

At 2 Tr 140-160, Ms. Wojtowicz provided testimony addressing Edison's generation, emission allowance expenses, and purchase power requirements for 2011 through 2015.   With regard to the expenses to be included in the PSCR factor, Ms. Wojtowicz states, at 2 Tr 141, that:

> The PSCR expense forecast includes the fuel expense for electric generation, purchased and renewable power expense, revenue from wholesale power sales to third parties, NO_x emission allowance expense associated with generation, SO_2 emission

> allowance expense associated with generation, bundled transmission expenses, MISO energy market and ancillary services market (ASM) related costs, and urea expense. The bundled transmission expenses are those expenses forecasted to be incurred to serve Detroit Edison's full service load customers and do not include any transmission expenses incurred by alternative electric suppliers (AESs) to serve Electric Choice customers.

Ms. Wojtowicz provides a number of 2011 to 2015 projections, presented in exhibits A-13 through A-20. In Exhibit A-13, she presents Edison's Projected Fuel, Net Purchase Power, and PSCR Expense forecast for 2011-2015.[3] In exhibit A-14, she presents Edison's Forecast of Plant Generation (2011-2015) and, in exhibit A-15, Edison's Summer Resource Plan (2011-2015).

At 2 Tr 160, Ms. Wojtowicz states:

> [T]he projection and expenses are reasonable and prudent. As has been previously described, the projection of Detroit Edison's generation and purchased power were developed from an economic dispatch forecast designed to reliably and economically serve the energy and demand requirements of the Company's customers based on fuel cost, electricity market costs, and emission allowance costs. The forecast was evaluated based on historical operation and expected changes due to maintenance schedules, fuel costs, market-based electricity prices and changes in Net System Output. The emissions were projected from the economic dispatch taking into account the market price of emission allowances required for generation. All relevant power supply elements were evaluated and reasonable and prudent projections were utilized to arrive at a reasonable and prudent power supply plan for Detroit Edison for 2011 and for the "out years" of 2012-2015.

[3] Shown on Exhibit A-13 are the annual summaries of: forecast generation (Exh A-14); fuel expense (Exh A-2); forecasted Ludington Losses; the Net Purchased Power and Expense forecast (Exh A-16); the emission allowance expense projections for seasonal NO_X allowances for the years 2011 – 2015 (Exh A-17); the emission allowance expense projections for annual NO_X allowances for the years 2011 – 2015 (Exh A-18); the emission allowance expense projections for SO_2 allowances for the years 2011 – 2015 (Exh A-19); the urea and powdered activated carbon expense projections (Exh A-20); the bundled transmission expense (Exh A-5); an expense adjustment for FERC wholesale firm sales; an expense adjustment for interruptible sales; a transmission expense adjustment for customers whose rates do not include the PSCR factor, and; the PSCR Fuel and Purchased Power Expense. Tr 2, p 141-142.

With the exception of NO_X emission allowance expenses and REF project related expenses, none of these figures are challenged and are accepted.

Ring-fencing

MCAAA's witness testified about the issue of "ring-fencing". Without accepting it as fact, the entirety of the testimony is reproduced below (citation omitted) and is found at 2 Tr 295-96:

> DECO is a subsidiary of DTE Energy, which also owns Michigan Consolidated Gas Company (Mich Con), and a number of unregulated subsidiaries and affiliates. In turn, and Mich Con also own subsidiaries and affiliates. [*sic*] This holding company structure inherently provides the framework and incentive for potential intercorporate transactions aimed at enhancing holding company consolidated profits at the expense of the regulated utility subsidiaries. Such transactions can in turn drive up the costs and rates of the regulated utilities, as holding company profits can be derived under the guise of utility costs, in some instances for services or products that are provided to the utility that are unnecessary or that are provided at an inflated cost or mark-up given that the transactions are not subject to the discipline of arms-length completive [*sic*] processes.
>
> Several utility commissions around the country are now instituting regulatory approaches referred to as "ring-fencing" to protect the utility from adverse impacts arising from intercorporate affiliated transactions or subsidies. The application of this regulatory tool is more fully described in the literature[1].
>
> In order to ensure that DECO's base and Act 304 rates are minimized and are just and reasonable, and that DECO's costs arise from reasonable and prudent activities, policies, and practices, the Commission should direct that "ring-fencing" approaches be instituted with respect to DECO. In addition, the Commission should undertake review and audit of certain of DECO's (and DTE and Mich Con) affiliates to ensure against potentially abusive intercorporate transactions that may adversely impact DECO's costs and rates. The Commission's authority to undertake such audits and reviews is well grounded in the state statutes applicable to the Commission, but are now also buttressed by the provisions of federal law, including Section 1265 of the Public Utility Holding Company Act of 2005, 42 USC 1261 et seq., which is a part of the Energy Policy Act of 2005 (EPACT). The need for these enhanced

> regulatory approaches is highlighted by examples of DECO's intercorporate transactions or proposals as discussed later in my testimony.
>
> [1] Maryland Commission Staff, "Commission Staff Analysis of Ring-Fencing Measures for Investor-Owned Electric and Gas Utilities", February 18, 2005; Paper on behalf of NARUC Staff Subcommittee on Accounting and Finance, "Ring Fencing Mechanisms for Insulating a Utility in a Holding Company System", circa 2004; Testimony of Marc Spitzer, Commissioner, Federal Energy Regulatory Commission, Before the Committee on Energy and Natural Resources, United States Senate, May 1, 2008.

Edison's witness, Mr. Johnston testified that he had reviewed the material referenced in the quoted footnote, above, and that he does not believe this is the proper proceeding to address "mechanisms designed to protect the financial liability of . . . Edison." 2 Tr 207. At 2 Tr 207-08, he adds that:

> To the extent that Mr. Peloquin believes that policies regarding the price at which products and services should be transferred between regulated and unregulated affiliates should be established or instituted in this proceeding, the Company believes that the MPSC-approved Code of Conduct (MPSC Case No. U-12134), the MPSC Affiliate Transaction Guidelines (MPSC Cases U-13502 and U-10149/U-10150), and FERC's Affiliate Restrictions (18 C.F.R. § 35.39, 18 C.F.R. § 35.44, and FPA § 203) adequately address those transactions. In addition to MPSC and FERC requirements, DTE Energy has internal procedures, attached as Exhibits A-22 and A-23, as well.

POSITIONS OF THE PARTIES

Introduction

Edison argues that it provided evidence to establish that its projected expense of $1,206,927,000 for generation, purchased power, emission compliance, and associated costs are reasonable and prudent and that there is "no evidence to the contrary". Edison Init Br, p 6. Edison asks the Commission to approve its 2011 power supply plan and five-year forecast. Edison Init Br, p 6. Specifically, Edison requests issuance of a Commission order, providing the following relief: approval of Edison's proposed Plan and for a levelized 2011 PSCR Factor of negative 2.98 mills/kWh in bills, from January 1, 2011 through December 31, 2011, inclusive of Edison's projected 2010 PSCR under-recovery of $36.349 million; approval of Edison's five-year PSCR forecast; approval of Edison's request to recover the incremental cost of urea, above or below that included in Edison's base rates; provide "concurrence", pursuant to MCL 460.6j(7), that the Commission is likely to permit the Company to recover the mercury emission-related expense for 2015; approval of the proposed Transfer Price treatment of renewable energy in Detroit Edison's PSCR process; approval of "all other proposals made by [Edison] in its testimony, exhibits, and in this Initial Brief, and; grant all other relief that the Commission deems appropriate. Edison Init Br, p 23-24.

Staff states that "after conducting a review of [Edison's PSCR Plan] and factor for the year 2011, Staff did not find the proposed PSCR plan and factor to be unreasonable or imprudent." Staff Rep Br, p 1.

There are, however, a number of unresolved issues presented by Staff and the intervenors, related to: ring-fencing, reduced emission fuel, NOx emission allowance costs, mercury emission reduction costs, and spent nuclear fuel costs. Each of these will be addressed separately, below.

Ring-Fencing

MCAAA argues that “that the Commission can and should scrutinize affiliated transactions in order to set and maintain reasonable rates.” MCAAA Init Br, p 19. At MCAAA Init Br, p 36-37, MCAAA describes ring-fencing, by stating:

> The regulatory tools known as "ring-fencing" . . . are described in the study formulated by the Maryland Public Service Commission . . . . This study summarizes ring-fencing as follows:
>
> > Ring-fencing is defined as the legal walling off of certain assets or liabilities within a corporation, as in a company forming a new subsidiary to protect (ring-fence) specific assets from creditors." Ring-fencing as a concept includes a number of measures that may be implemented to protect the economic viability of utility companies and their affiliates within a holding company structure. Ring-fencing measures are intended to insulate a regulated utility from the potentially riskier activities of an unregulated affiliate. Insulting [*sic*] the utility is intended to ensure the financial stability of the utility and the reliability of its service.

MCAAA argues that “these studies . . . demonstrate the kind of scrutiny and remedial measures that are available to protect ratepayers from [the] adverse [effects] that can result from affiliated transactions.” MCAAA Init Br, p 45. MCAAA believes ring-fencing should be applied to minimize costs and to ensure rates are the result of reasonable and prudent policies and practices. MCAAA Init Br, p 45.

“MCAAA recognizes that these measures may relate more to base rate regulation than to Act 304 regulation. However, affiliated transactions can and do affect Act 304 costs also and so these measures have relevance to Act 304 regulation”. MCAAA Init Br, p 36.

Edison argues that the MCAAA "does not explain the concept of 'ring fencing' or how it applies to Detroit Edison and instead merely refers to three documents that are not part of the record and asks that the Commission adopt 'ring fencing'." Edison Init Br, p 13. Edison adds, at Edison Init Br, p 14 (citations omitted):

> "[R]ing fencing" and other similar policy debates are not relevant to [and have] no consequence to the determination of the issues in this PSCR Plan proceeding, which is being held pursuant to the unambiguous statutory language of Act 304 to address Detroit Edison's expected sources of electric power supply for the 2011 PSCR Year and 5 year forecast. Policy debates about "ring fencing" and documents . . . not admitted in this record are of no consequence to determining this Act 304 proceeding.

Edison adds, at Edison Rep Br, p 17-18, that:

> [T]o the extent that [MCAAA] believes that policies regarding the price at which products and services should be transferred between regulated and unregulated affiliates should be established or instituted in this proceeding, the Company believes that the MPSC-approved Code of Conduct (MPSC Case No. U-12134), the MPSC Affiliate Transaction Guidelines (MPSC Cases U-13502 and U-10149/U-10150), and FERC's Affiliate Restrictions (18 C.F.R. § 35.39, 18 C.F.R. § 35.44, and FPA § 203) adequately address those transactions. In addition to MPSC and FERC requirements, DTE Energy has internal procedures, which are set forth in Exhibits A-22 and A-23 . . . .

<u>Reduced Emission Fuel Project</u>

Edison argues that its "sale of coal to its affiliate, SCFC, and subsequent re-sale of coal from SCFC to Edison along with the addition of the refined coal adder, is consistent with the Code of Conduct and in the best interest of its customers." Edison Init Br, p 16. Edison continues, at Edison Init Br, p 16 (citations omitted), by arguing that:

> [Edison] clearly explained . . . that all affiliate transactions related to Edison's REF are . . . consistent with Edison's Code of Conduct . . . and . . . properly includable in Edison's fuel inventory for recovery through the PSCR process. Edison's REF addresses NO_X and SO_2 emission allowances, the cost of fuel burned, payment to P. A. 2 suppliers, and the future consumption of powdered activated carbon to dispose of fuel burned, all of which are clearly PSCR and Act 304 costs.

MCAAA considers Edison's proposed REF Project to be a "prime example of a questionable affiliated transaction". MCAAA Init Br, p 45. MCAAA believes the "best protection for ratepayers" is to not approve "any arrangement whereby an unregulated affiliate would be injected into the fuel handling or processing function". MCAAA Rep Br, p 19. MCAAA considers, "irrelevant", Edison's claim that the Project is consistent with the Code of Conduct. MCAAA Rep Br, p 19. For MCAAA, "[w]hether or not a transaction falls within the Code of Conduct does not establish that the resulting costs are reasonable and prudent . . . and does not . . . establish that [Edison] is taking all measures to minimize its costs". MCAAA Rep Br, p 19.

MCAAA argues, at MCAAA Init Br, p 48-49:

> [Edison's Project] should be rejected for several reasons . . . . First, DECo has presented far too little information as to what is involved in this proposal, and why the functions . . . should be assigned to a DTE affiliate rather than . . . undertaken by DECo itself.
>
> Second, . . . there would be multiple opportunities for the unregulated DTE affiliate . . . to reap significant profits from the activity, which would then be included . . . in PSCR rates at the expense of customers. . . .
>
> Third, the REF proposal is not a category of expense to be included in a PSCR Plan, and is therefore beyond the scope of a Plan case . . . .
>
> Fourth, inclusion of REF costs in this Plan would constitute poor public policy and precedent. This program if adopted could turn out to be a huge expense boon-dogle and could serve as the

model for additional affiliated transaction proposals which could intrude into the Act 304 process and drive up costs.

Fifth, these kind of fuel handling activities are subject to the restrictions and prohibitions found in Section 6j(13)(d) and (e), MCL 460.6j(13)(d) and (e), which state in part:

> (13) In its order in a power supply cost reconciliation, the commission shall:
>
> * * *
>
> (d) Disallow transportation costs attributable to capital investments to develop a utility's capability to transport fuel or relocate fuel at the utility's facilities and disallow unloading and handling expenses incurred after receipt of fuel by the utility.
>
> (e) Disallow the cost of fuel purchased from an affiliated company to the extent that such fuel is more costly than fuel of requisite quality available at or about the same time from other suppliers with whom it would be comparably cost beneficial to deal.

In response, Edison argues, at Edison Rep Br, p 18-20 (citations omitted), that:

> Contrary to . . . MCAAA's contention that Edison presented insufficient information, the evidentiary record shows . . . that . . . there were a number of reasons why Detroit Edison's affiliates . . . were selected to design, construct, own and operate the REF processing facilities. First and foremost was the fact that the arrangements provided Detroit Edison a risk free option to help it attain the mercury emission reduction requirements contained in Michigan Rule 1503 beginning in 2015. Detroit Edison was not required to make any capital investment to support the REF processing and therefore did not assume any risk that the REF project was not successful. Detroit Edison reasonably determined that the tax risks and commitment to a technology that was unproven at its generating facilities were not appropriate for a regulated utility.
>
> . . . DTE Energy Services ("DTEES"), the parent company of both BRFC and SCFC, has experience designing, constructing, and operating the production equipment and was willing to take on the associated risk. At the time the REF facilities were constructed at the Belle River and St. Clair Power Plants, the existing legislation required the facilities to achieve commercial operation by January 1, 2010 and Detroit Edison had only a limited time to pursue alternative processes or suppliers. Further, Detroit Edison was not

> aware of any other supplier that was willing to make this type of investment at the time the REF project needed to move forward given the existing legislation.
>
> . . . [A]t the time that Detroit Edison entered into discussions with DTEES for the provision of REF for Belle River Power Plant, DTEES was one of only three known licensees for the provision of the proprietary technology and DTEES held a license to use the unique and proprietary chemical additive technology at Detroit Edison sites. DTEES had been evaluating Hg technologies for more than two years and through August 2009 made a significant investment in the evaluation and testing of multiple technologies.
>
> Finally, . . . the REF arrangement made sense since DTEES had already reached a similar agreement with the Michigan Public Power Agency ("MPPA"), a partial owner of the Belle River Power Plant. In addition, the DTEES proposal provided the following:
>
> (a) Reduction in Detroit Edison's working capital expense by not carrying coal inventory;
>
> (b) Reduction in NO_X emission allowance expense; and
>
> (c) PSCR customers will never pay more than their environmental benefits.

With regard to MCAAA's second point, Edison argues, at Edison Rep Br, p 21-22, that:

> MCAAA essentially argues that Edison's REF coal inventory transactions between St. Clair Power Plant ("SCPP") and Edison's affiliate, St. Clair Fuels Company ("SCFC") creates issues under the Code of Conduct. However, the evidentiary record does not support MCAAA's erroneous reasoning or allegations.
>
> For instance, . . . Edison's sale of coal to its affiliate, SCFC, and subsequent re-sale of coal from SCFC to Edison along with the addition of the refined coal adder, is consistent with the Code of Conduct and in the best interest of its customers. . . . [T]he Commission has routinely reviewed any and all costs resulting from affiliate transactions in the annual PSCR reconciliation filings. No products or services related to the REF proposal are being provided to Detroit Edison from any of its affiliates which reflect any inflated costs or markups. Detroit Edison has been provided a risk-free option at no increased cost to its PSCR customers to reduce emission compliance expense. To the extent that the REF proposal provides one of its affiliates the potential to recover its revenue requirement for the REF facilities it has constructed, the basis for calculating the return on their "rate base" is Detroit Edison's currently authorized overall ROR of 7.02%, which has been determined to be reasonable for a regulated utility. However,

as can be plainly seen on Exhibit A-21, SCFC is not able to recover its entire revenue requirement in any of the years 2011 through 2015. . . . Once the plants experience reduced emissions, the cost of the Refined Coal Adder will be no greater than the benefits of the reduced emission allowance expense capped at the amount of the revenue requirement associated with the REF Project facility. Once the cost of the Refined Coal Adder reaches this cap, any additional benefits of reduced emission allowances will flow directly through to the PCSR customers. In summary, the cost of the Refined Coal Adder, if any, will be entirely offset by a corresponding savings in PSCR emissions allowance expense." Thus, the evidentiary record shows that there is no merit to MCAAA's assertions that Edison's REF proposal would facilitate the transfer of Edison's purchased coal inventories to the DTE affiliate which would then process the coal and sell it back to Edison at an unregulated or higher price.

In response to MCAAA's third point, Edison argues, at Edison Rep Br, p 22-23, that the:

> REF is . . . properly includable in Edison's fuel inventory for recovery through the PSCR process. . . . The single largest benefit for Detroit Edison from implementing this project is the ability to reduce mercury reduction compliance costs beginning in 2015, the first compliance year for Michigan Rule 1503. In addition, there are benefits to Edison's customers that flow through the non-PSCR rates. For example, the ability to reduce working capital associated with coal inventory and the ability to possibly continue making fly ash sales helped this agreement move forward. Finally, the fact that Detroit Edison's arrangements were modeled after those between BRFC and MPPA, a partial owner of the Company's Belle River Power Plant, provided additional support. Thus, Edison's REF addresses NO_X and SO_2 emission allowances, the cost of fuel burned, payment to P. A. 2 suppliers, and the future consumption of powdered activated carbon to dispose of fuel burned, all of which are clearly PSCR and Act 304 costs.

Edison argues that MCAAA's fourth and fifth points, above, are "redundant of the second and third" points and that MCAAA "provides no analysis whatsoever to support its vague and unspecified concerns and assertions".

Edison Rep Br, p 23. Edison considers them "wholly devoid of any merit." Edison Rep Br, p 23.

NO_x Adjustment

MCAAA argues for a "downward adjustment of $3,319,170 related to the calculation of NO_x allowance purchase costs." MCAAA Init Br, p 50. MCAAA argues that, because of the "extra-ordinary high cost of some of Edison's NO_x allowance purchases", the 2011 PSCR Plan expenses should be reduced and Edison should "attempt to justify these exorbitant purchases in the reconciliation phase of this case." MCAAA Init Br, p 51-52.

In response, Edison argues that, in 2008, it purchased 2011 NO_x seasonal and annual emission allowances in accord with the "pre-purchase strategy" it outlined in its 2008 PSCR Plan case, Case No. U-15417. Edison Rep Br, p 24. Edison states that these 2008 purchases were made at the, "then-current market prices for 2011" emission allowances. Edison Rep Br, p 24. Edison adds, at Edison Rep Br, p 24-25, that:

> 2011 NO_x emission allowance prices are much lower now than they were in 2008. . . . [I]n July 2008, the D.C. Circuit Court vacated the Clean Air Interstate Rule (CAIR) . . . . NO_x emission allowance prices dropped significantly after CAIR was vacated. In late 2008, the U.S. economy went into a deep recession, which resulted in decreased electricity demand [and less NO_x emission]. The excess supply of NO_x emission allowances caused the decrease in price. These . . . events . . . were unpredictable and validate the Company's "dollar cost averaging" approach to emission allowance acquisition. NO_x emission allowance prices have been very volatile since 2008 with annual NO_x emission allowances ranging from as high as about $5600 all the way down to the current low of about $250. In that same period, seasonal NO_x allowances have been as high as about $1400 and as low as about $25. . . . Thus, the Company's decision to pre-purchase

> allowances . . . in accordance with its pre-purchase strategy . . . was reasonable and prudent.

MCAAA counters by arguing that Edison's claims regarding its pre-purchase strategy and benefits to customers are made without "explanation or citation". MCAAA Rep Br, p 20. MCAAA adds, at MCAAA Rep Br, p 20-21, that:

> [Edison] does not show that its huge costs for these allowances, compared to present costs to purchase said allowances, is consistent with the standards of reasonableness and prudence and cost minimization. . . . .
>
> Moreover, it appears that DECO may be claiming a cost which is not within the scope of this Plan case for 2011, for at least two reasons: The claimed costs do not comport with 2011 costs for these emission allowances . . . and because, if the costs related to that incurred in 2008 (as DECo intimates), the costs are not relevant to this case for 2011.
>
> The ALJ and the Commission should adopt the downward rate adjustment proposed by MCAAA on the emission allowance costs and also issue a Section 7 warning that the Commission is not likely to approve these costs in the reconciliation case, and directing DECo to present more information on this issue.

Spent Nuclear Fuel (SNF)

MCAAA recommends disallowance of the one mill per kWh fee collected and transferred to the federal government for the final disposal of SNF. MCAAA Init Br, p 1. In the alternative, MCAAA recommends these funds be directed to a "SNF fee trust". MCAAA Init Br, p 1-2. MCAAA argues for the disallowance of the trust "on a prospective basis, pending a showing by DECo of efforts to seek appropriate contract remedies to protect the funds." MCAAA Init Br, p 1-2.

The MCAAA adds, at MCAAA Init Br, p 17, that:

> It is clear that the federal SNF program has been obliterated. In the face of these developments, DECo must be held to a higher

> standard of action to enforce its Standard Contract and to seek additional contract remedies such as restitution and refund of fees in addition to damages on [a] going-forward basis. DECo could also seek the establishment of an escrow trust or add the fee payments to its damage claims. In the meantime, the Commission should require that all perspective SNF fee charges to ratepayers be disallowed in rates or be placed in an external MPSC-regulated trust.
>
> [Edison's filing] is . . . quite sparse, and reveals no new strategy, or action being planned or being undertaken . . . . The Company's overall approach seems to remain incurring additional costs due to the federal breach . . . and to pass on all costs to the ratepayers. . . .
>
> [Edison's] approach is unreasonable and imprudent, and places Michigan's ratepayers and taxpayers, and the public interest, at enormous risk. The Commission should undertake prompt action . . . to protect the ratepayers, taxpayers, and the public interest . . . .

Edison argues that it has acted "responsibly and reasonably" to address the issue. Edison Init Br, p 18. Edison points to its continuing pursuit of "damages against the DOE", its "very effective [management of] its nuclear fuel expense", "a conservative and graduated approach to manage on-site spent fuel storage", and its "engage[ment] in political initiatives". Edison Init Br, p 19. Edison believes SNF storage is a "national issue" and that's its actions are "in line with . . . other U.S. nuclear utilities." Edison Init Br, p 19. Edison adds, at Edison Init Br, p 19 (citations omitted), that:

> MCAAA simply rehashes the same arguments that MEC/PIRGIM repeatedly presented . . . through the same counsel and witness. The Commission consistently rejected those arguments and was consistently upheld on appeal.[4] The Commission has repeatedly recognized that SNF disposal is a

[4] To support its argument Edison cites, among other cases, Case No. U-12613, Case No. U-13808, Case No. U-15244, Case No. U-15245, and *In re Application of Detroit Edison Co*, 276 Mich App 216 (2007). Edison Init Br, p 19-21. MCAAA, however, argues that these cases are not binding and that there has been a "major change of circumstances" because the "federal government is now in total breach of its statutory and contractual duties to dispose SNF". MCAAA Rep Br, p 12.

> national problem and that Michigan utilities must comply with federal law.

Edison continues by arguing, at Edison Init Br, p 22 (citation omitted) that:

> [T]he suggestion that Edison should withhold nuclear waste fees . . . could result in Edison being found in default of its contract with the DOE. Section 302(b) of the Nuclear Waste Policy Act requires the holders of nuclear power plant operating licenses to enter into the Standard Contract with the DOE. . . . If Edison were to be found in default on its contract by not paying fees into the nuclear waste fund . . . Edison would risk the NRC's denial of license amendments necessary to operate the Fermi plant, and could jeopardize Edison's lawsuits for damages against the DOE.
>
> There continues to be no merit in the suggestions . . . that Edison could pay the DOE and place an additional amount in a trust fund . . . . Such an action and corresponding cost increase would not be in the best interests of Edison or its customers. SNF is a national issue that the federal government has obligations and incentives to resolve, so it is reasonable to expect that the federal government will eventually accept SNF for disposal. Therefore, placing nuclear waste fees in a trust fund is unreasonable and not necessary to protect customers from default by the federal government.

Edison adds, at Edison Rep Br, p 10-11, that:

> [It] has no option, short of violating federal law . . ., but to pay the federally-mandated charge.
>
> * * *
>
> [T]he Commission cannot prevent Edison from receiving full and timely recovery of the mandatory SNF fees and costs from its customers. Both state and federal courts have consistently held that a state utility commission setting retail rates must allow, as reasonable operating expenses, any costs incurred by a utility pursuant to federal mandate.

In response, MCAAA argues that Edison "holds to the outdated fantasy that the federal government has held to the commitment to dispose of SNF." MCAAA Rep Br, p 3. MCAAA argues that, through its "actions and pronouncements", the federal government has made "clear" that it has "totally breached its statutory and contractual obligations to dispose of SNF." MCAAA Rep Br, p 3. MCAAA argues that the "fact that SNF disposal issues are 'national in scope' does not detract from the fact that [Edison] . . . has a Standard Contract . . . requiring the federal government to dispose SNF in exchange for the SNF fee payments . . . ." MCAAA Rep Br, p 4. As MCAAA sees it, Edison "should act more diligently to seek all possible legal and equitable remedies to enforce the Standard Contract and to protect the fees it is paying . . . to the federal government." MCAAA Rep Br, p 5. MCAAA argues that Edison has provided no "justification for its not taking further steps to enforce its contract and to protect the fees, including seeking restitution or refund of all past and ongoing fees paid under the contract, or at minimum, seeking a separate external escrow trust to receive all said fees pending any potential future performance of SNF disposal under the contract." MCAAA Rep Br, p 5.

Finally, at MCAAA Rep Br, p 13-14, MCAAA argues that its recommendations are "measured and balanced" and explains, that:

> An escrow trust . . . does not absolve the ratepayers for paying for the SNF disposal . . . . Rather, the ratepayers continue to fund the fees, but the fee funds are protected by being placed in trust to ensure that the funds are preserved to accomplish the purpose for the fee collections, namely, SNF disposal, and also to assure that ratepayers will not be charged duplicative times for the same expense and to cover the federal breach. Escrow trusts are long recognized in commercial transactions as a fair and balanced means to protect all parties to a contract, and no reason exists to waive such a remedy here in view of the dramatic and clear breach of the Standard Contract, and the lack of adequate (reasonable and prudent) responsive action by DECo to address the default.

Staff notes that this matter has been previously adjudicated before the Commission and in the courts. Staff Rep Br, p 4. Staff states that the

"Commission has repeatedly recognized that SNF disposal is a national problem, and that Michigan utilities must comply with the federal law."[5] Staff Rep Br, p 4. Staff continues by arguing that MCAAA has presented nothing that would warrant the Commission's review of its prior decisions on this issue and "recommends that the Commission . . . reject MCAAA's request to have Detroit Edison default on its contract with the federal government and place prospective nuclear waste fees in a trust." Staff Rep Br, p 7.

Mercury Costs

Staff opposes Edison's request for "Commission concurrence that it is likely to permit the Company to recover its mercury emission-related expense for 2015." Staff Rep Br, p 3. Staff argues that, under MCL 460.6j(7), the "Commission evaluates the Company's 5-year forecast but does not pre-approve the items it contains." Staff Rep Br, p 4.

The Attorney General agrees with Staff and adds, at AG Init Br p 3-4, that:

> [T]he language in MCL 460.6j(7) limits the scope of the Commission's decisions to the power to issue warnings about potential future disallowances based upon present forecast evidence. Thus, the Commission is not statutorily authorized to pre-approve a forecast or a portion of a forecast as DECo is requesting.
>
> . . . [A]pproval would be premature, and this approval would be the equivalent of allowing recovery of fuel handling expense despite the provisions in MCL 460.6j(13)(d).
>
> . . . MCL 460.6j(7) does not authorize the MPSC to approve or disapprove elements of a forecast that fall beyond the plan year being reviewed under MCL 460.6j(6).

[5] For support, Staff cites to the Commission's November 20, 2001 order in Case No. U-12613, its November 23, 2004, and June 30, 2005, orders in Case No. U-13808, and *In re Application of Detroit Edison Co*, 276 Mich App 216 (2007).

* * *

> [Therefore, the] Attorney General requests the Administrative Law Judge to issue a proposal for decision that recommends denying the requests for pre-approval of future portions of the Company's 5-year forecast because MCL 460.6j(7) does not authorize the Commission to approve or disapprove portions of a forecast. In addition, ... the evidence regarding such plans has not been sufficiently developed to permit the Commission to make a reasoned conclusion about whether such plans will become reasonable and prudent.

ABATE "agrees with the Attorney General's position". ABATE Rep Br, p 1.

At Edison Rep Br, p 2 (citations omitted), Edison argues that the Attorney General's position "is meritless for two reasons" and explains:

> First, notwithstanding the AG's mischaracterization of Edison's request, the Company is not seeking any pre-approval of any cost item from its 5-year forecast, but is merely seeking the Commission's evaluation of whether it is likely or unlikely to permit the Company to recover the mercury emission-related expense for 2015. Second, the AG is contradicted by the express language of MCL 460.6j(7), which states:
>
>> "In its final order in a power supply and cost review, **the commission shall evaluate** the decisions underlying the 5-year forecast filed by a utility pursuant to subsection (4). **The commission may also indicate** any cost items in the 5-year forecast that, on the basis of present evidence, the commission would be **unlikely** to permit the utility to recover from its customers in rates, rate schedules, or power supply cost recovery factors established in the future."
>
> * * *
>
> [T]he plain and ordinary language of MCL 460.6j(7) does not merely limit the Commission to "issue warnings about potential future disallowances based upon present forecast evidence" as suggested by the AG. In fact, this statutory provision requires the Commission to evaluate a utility's 5-year forecast and provides that the Commission "may also indicate" the likelihood of future recovery of a cost item in the 5-year forecast. This is exactly what Edison is requesting in its Application with respect to the mercury emission-related expense for 2015.

DISCUSSION

Statutory Provisions

MCL 460.6j provides, in part:

> (2) . . . [T]he public service commission may incorporate a power supply cost recovery clause in the electric rates or rate schedule of a utility. . . . Any order incorporating a power supply cost recovery clause shall be as a result of a hearing solely on the question of the inclusion of the clause in the rates or rate schedule . . . .
>
> (3) In order to implement the power supply cost recovery clause . . ., a utility annually shall file . . . a complete power supply cost recovery plan describing the expected sources of electric power supply and changes in the cost of power supply anticipated over a future 12-month period specified by the commission and requesting for each of those 12 months a specific power supply cost recovery factor. . . . The plan shall describe all major contracts and power supply arrangements entered into by the utility for providing power supply during the specified 12-month period. The description of the major contracts and arrangements shall include the price of fuel, the duration of the contract or arrangement, and an explanation or description of any other term or provision as required by the commission. The plan shall also include the utility's evaluation of the reasonableness and prudence of its decisions to provide power supply in the manner described in the plan, in light of its existing sources of electrical generation, and an explanation of the actions taken by the utility to minimize the cost of fuel to the utility.
>
> (4) In order to implement the power supply cost recovery clause . . ., a utility shall file . . . a 5-year forecast of the power supply requirements of its customers, its anticipated sources of supply, and projections of power supply costs, in light of its existing sources of electrical generation and sources of electrical generation under construction. The forecast shall include a description of all relevant major contracts and power supply arrangements entered into or contemplated by the utility, and such other information as the commission may require.
>
> (5) If a utility files a power supply cost recovery plan and a 5-year forecast . . ., the commission shall conduct a proceeding . . . for the purpose of evaluating the reasonableness and prudence of the power supply cost recovery plan filed by a utility . . . and establishing the power supply cost recovery factors to implement a

> power supply cost recovery clause incorporated in the electric rates or rate schedule of the utility. . . . .
>
> (6) In its final order in a power supply and cost review, the commission shall evaluate the reasonableness and prudence of the decisions underlying the power supply cost recovery plan filed by the utility . . . and shall approve, disapprove, or amend the power supply cost recovery plan accordingly. In evaluating the decisions underlying the power supply cost recovery plan, the commission shall consider the cost and availability of the electrical generation available to the utility; the cost of short-term firm purchases available to the utility; the availability of interruptible service; the ability of the utility to reduce or to eliminate any firm sales to out-of-state customers if the utility is not a multi-state utility whose firm sales are subject to other regulatory authority; whether the utility has taken all appropriate actions to minimize the cost of fuel; and other relevant factors. The commission shall approve, reject, or amend the 12 monthly power supply cost recovery factors requested by the utility in its power supply cost recovery plan. The factors shall not reflect items the commission could reasonably anticipate would be disallowed under subsection (13). The factors ordered shall be described in fixed dollar amounts per unit of electricity, but may include specific amounts contingent on future events.
>
> (7) In its final order in a power supply and cost review, the commission shall evaluate the decisions underlying the 5-year forecast filed by a utility . . . . The commission may also indicate any cost items in the 5-year forecast that, on the basis of present evidence, the commission would be unlikely to permit the utility to recover from its customers in rates, rate schedules, or power supply cost recovery factors established in the future.

Ring-Fencing

As Edison observes, MCAAA "does not explain the concept of 'ring fencing' or how it applies to Detroit Edison and instead merely refers to three documents that are not part of the record and asks that the Commission adopt 'ring fencing'." Edison Init Br, p 13. Also, as even MCAAA suggests, pursuant to MCL 460.6j, this matter is outside the proper scope of this hearing. Therefore, based on the record and the law, MCAAA's request that the Commission adopt "ring-fencing" is denied.

Reduced Emission Fuel Project

Included in the Plan and the five-year forecast is Edison's Reduced Emission Fuel Project and its associated costs. Edison asks for Commission approval of the Project as part of its Plan. In addition, Edison requests that the Commission enter an order, pursuant to MCL 460.6j(7), stating that it is likely to permit Edison to recover its REF mercury emission related expenses for 2015.

MCAAA opposes inclusion of the Project in the Plan and considers it to be a "questionable affiliated transaction" that should be categorically denied because it would allow an unregulated affiliate to become part of the fuel handling and processing procedures. MCAAA finds further fault with the Project because, it believes, Edison has presented too little information about the Project and because it would permit the affiliated entities to profit from PSCR rates and drive up costs. MCAAA also questions whether REF cost recovery would be disallowed under MCL 460.6j(130(d) and (e). For many of the reasons cited by MCAAA, the Plan should be modified to exclude approval of the Project.

MCAAA is correct that the REF project represents a questionable affiliate transaction. Under the Plan, Edison proposes to transform a PSCR cost, i.e. SO_2 emission allowance cost[6], into a revenue stream for its unregulated affiliate. However, Edison's presents little more than a sketch of the business relationships that have been created and the processes involved.

[6] In addition, in its five-year forecast, Edison proposes to extend this relationship to mercury emission reduction costs.

As an example, I am unable to find, anywhere in the record, the actual contractual arrangements between Edison and its affiliates. Additionally, very little is presented to explain the relationship between Edison, the Michigan Public Power Agency (MPPA), and the Belle River Fuels Company. Rather than developing a well documented evidentiary record to explain this relationship, Edison has only touched upon the subject. In addition, Edison claims that because of the, then existing legislation, it had a limited time to pursue alternative processes or suppliers. Edison provides no information regarding the alternative processes and suppliers from which one might compare the processes and services provided by its affiliates. Furthermore, Edison has indicated that it will provide "coal handling", "consulting", and "other services" to the Fuels Companies at "Edison's cost". The record does not provide details regarding the nature of these services, who will be providing them, and what Edison's costs are. It is not clear how these costs will be accounted for and if any will flow through to non-Edison entities, such as MPPA. Additionally, MCAAA argues for rejection of the REF because recovery of some of its costs would be barred by MCL 460.6j(13). Unfortunately, the record is not sufficiently developed to allow for a determination on this issue.

If Edison wishes Commission approval of the REF project's business arrangements, it needs to build a thorough evidentiary record detailing and explaining exactly the business model it is proposing. It has clearly not done so in this case. Rather, Edison has provided a general overview of the REF Project that leaves many unanswered questions. For possible approval by the Commission, Edison should more fully develop the record in its next Plan case.[7]

With regard to the five-year forecast, Staff, the Attorney General, and ABATE argue that Edison is asking for pre-approval of this expense and that such pre-approval is not permitted under MCL 460.6j(7). However, Edison's request is not a request for the pre-approval of a 2015 power supply cost, as the parties have characterized it[8].

Pursuant to MCL 460.6j(7):

> [T]he commission shall evaluate the decisions underlying the 5-year forecast . . . [and] may also indicate any cost items in the 5-year forecast that, on the basis of present evidence, the commission would be unlikely to permit the utility to recover from its customers in rates, rate schedules, or power supply cost recovery factors established in the future.

Edison's request is permissible under MCL 460.6j(7). In this order, the Commission is statutorily required to "evaluate the decisions underlying the 5-year forecast". Most certainly, this statutory requirement permits Commission comment upon the cost items in the forecast. It is without doubt the Commission

[7] It is worth noting that, for the Plan year, Edison proposes to provide the benefit of reduced SO_2 and NO_X emissions without additional cost to its customers. Thus, while the REF project is not approved, its expenses may be reasonable and considered in the reconciliation process.

[8] It is noted that Edison makes a general request for approval of its five-year forecast. However, "Act 304 does not require the Commission to approve, disapprove, or modify the five-year forecast in the same way that it adjudicates the immediate plan year." *In re Wisconsin Electric Power Co*, U-12615, Opinion and Order, p 20 (November 20, 2001). Furthermore, "nowhere is the Commission authorized to either reject or demand the re-filing of a utility's five-year forecast." *In re Consumers Power Co*, U-10710, Opinion and Order, p 12 (December 20, 1995). While not necessary for resolution of this matter, it is reasonable to conclude that, by analogy, the Commission is not authorized to approve a five-year forecast. "The real value of the five-year forecast is in providing a context for the determinations required by the plan and as a means of giving advance notice of forward-looking developments that the Commission may wish to evaluate now in order to provide guidance for future decision-making." *In re Wisconsin Electric Power Co*, U-12615, Opinion and Order, p 20 (November 20, 2001). Thus, in the context of a Plan case, the five-year forecast "should be accepted for filing". See *In re Consumers Power Co*, U-10710, Opinion and Order, p 22 (December 20, 1995).

may indicate any costs items for which it would be unlikely to permit recovery. It is equally doubtless that, in the process of evaluating the forecast, the Commission has authority to comment upon the forecasts' reasonableness and to indicate costs for which, under the present evidence and circumstance, it is likely to permit recovery. By providing such guidance, the Commission is not pre-approving a cost, as Staff, the Attorney General, and ABATE argue, but rather is exercising an inherent, but not necessary, component of the Commission's statutorily mandated power to evaluate the forecast.

While the Commission has the authority to grant Edison's request, such relief is, at best for Edison, premature. In addition to the Plan related evidentiary shortcomings stated, above, Edison admits that the REF is in the "early testing phases" and that it "continues to evaluate REF" as a means to minimize mercury emissions costs. When Edison is able to provide actual data regarding the REF's efficacy, the Commission will be better able to make a determination regarding recoverability of the associated costs. Edison has not provided a sufficiently developed record to warrant the relief that it requests, i.e. a Commission proclamation that it is likely to permit Edison to recover its mercury emission related expenses for 2015.

NO_x Adjustment

MCAAA argues for a Plan amendment to remove $3,319,170 in NO_x allowance purchase costs. Based on the record presented, it appears that, pursuant to its pre-purchase strategy[9], Edison reasonably incurred these expenses from the purchase, in 2008, of 2011 NO_x allowances, at the, then, current market price. However, since 2008, because of certain court decisions and the recent economic meltdown, the price of these allowances has dropped greatly. MCAAA has presented no evidence to suggest Edison's pre-purchase strategy was unreasonable, that it was not followed, or that the steep decline in prices could have been anticipated. MCAAA's argument rests solely on the difference in the price of 2011 allowances, purchased in 2008, and the price at which they can be purchased, today. Without more, I find MCAAA's argument unconvincing and can not adopt its recommended amendment to the Plan. Based on the record presented, Edison reasonably incurred these costs and they should be included in the Plan.

<u>Spent Nuclear Fuel (SNF)</u>

MCAAA recommends amendment of the Plan to remove the one mill per kWh fee collected and transferred to the federal government for disposal of SNF. Alternatively, MCAAA recommends these funds be directed to a "SNF fee trust". Edison argues that it has acted reasonably to address the issue by pursuing damages against the DOE, by effectively managing its nuclear fuel storage expense, and by involvement in political initiatives.

This issue has been extensively litigated before the Commission, on numerous occasions. The Commission has consistently and correctly rejected

[9] For a description of the strategy, see Case No. U-15417, 3 Tr 259-63. The Commission discussed the strategy and approved Edison's power supply cost recovery plan in *Application of the Detroit Edison Co*, U-15417, Opinion and Order (January 13, 2009).

MCAAA's position[10]. No material changes of fact or law have been presented to warrant any change in the Commission's long-standing position. In short, these costs are mandated under federal law and, therefore, it is reasonable and prudent for Edison to collect and remit them to the federal government. This aspect of the Plan is approved with encouragement that Edison continue seeking appropriate legal actions to protect the interests of its customers.[11]

CONCLUSION

Edison's Application and accompanying evidentiary presentation meets the minimal filing requirements of MCL 460.6j.

Pursuant to MCL 460.6j(6), the reasonableness and prudence of Edison's Plan has been evaluated and, for the reasons and in the manner, stated above, Edison's Plan, including the PSCR factors, is approved, as amended.

Pursuant to MCL 460.6j(7), the decisions underlying the five-year forecast have been evaluated and the five-year forecast is accepted for filing.

Any arguments not specifically addressed in this Proposal for Decision were deemed irrelevant to the findings and conclusions of this matter.

---

[10] See Case No. U-12613, Case No. U-12614, Case No. U-12615, Case No. U-12725, Case No. U-13771, Case No. U-13808, Case No. U-13917, Case No. U-13919, Case No. U-15244, Case No. U-15245, *In re Application of Detroit Edison Co*, 276 Mich App 216 (2007), and *In re Application of Indiana Michigan Power Co*, 275 Mich App 369 (2007).

[11] In its next Plan case, Edison is encouraged to discuss the propriety of MCAAA's proposal as a potential remedy in any currently pending or future litigation against the federal government.

MICHIGAN ADMINISTRATIVE HEARING SYSTEM
For the Michigan Public Service Commission

Mark Eyster

Digitally signed by Mark Eyster
DN: cn=Mark Eyster, c=US, email=eysterm@michigan.gov
Date: 2011.09.30 12:36:19 -04'00'

Mark D. Eyster
Administrative Law Judge

ISSUED AND SERVED: September 30, 2011
drr